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SUBJECT: Santa Catarina - Port Development and Challenges

Reftels: A) 05 Sao Paulo 1307; B) 05 Sao Paulo 1106

11. SUMMARY. The Port of Itajai's phenomenal growth, the development of a competing port in the neighboring city of Navegantes, and the 2005 opening of a private port facility in Itapoa highlight the southern Brazilian state of Santa Catarina's prominent role in Brazilian trade. A U.S. company, Port Security International, has partnered with the Port of Itajai to make it the first port in Brazil to conduct scanning of inbound containers in an attempt to deter importation of counterfeit products and other contraband as well as evasion of taxes and customs duties. END SUMMARY.

Santa Catarina's Port Profile

12. During a recent visit to the small but economically vibrant southern state of Santa Catarina (population 5.4 million, 2004 GDP of 21.9 billion, area 95,000 square kilometers - about the size of Indiana), Consul General (CG) McMullen and EconOff Neel visited the city of Itajai, home to Brazil's third largest port. During the course of the visit, they met with the mayors of Itajai and neighboring city Navegantes and visited the Port Authority. CG signed a Networking with the USA (NUSA) agreement with the Port of Itajai on behalf of the Foreign Commercial Service (ref A). Currently, Santa Catarina has four ports:

- Itajai, with a volume of 675,000 container units a year, is the state's largest port. Its primary cargo is meat, sugar, ceramics, paper, machinery, chemicals, containers, and wood.
- Itapoa, the northernmost port in the state, began operating in August 2005. By its third year of operation, the port is expected to have a volume of approximately 300,000 container units per year, increasing to 500,000 per year by its fifth year of operation. Built at a cost of USD 100 million, Itapoa is currently the only private port in Santa Catarina. 55 percent of the construction cost was financed by the Inter-American Development Bank (IADB), the remaining financing came from Santa Catarinense investor Grupo Batistella, and two silent foreign investors. Itapoa's primary cargo is wood, machinery, and meat.

- Sao Francisco do Sul, with a container volume of 280,000 units per year, is the port closest to Joinville, Santa Catarina's largest city (population 500,000) and the state's primary industrial pole. The port's primary cargo is soy oil and chaff, barley, and steel. Although Sao Francisco do Sul is the closest port to Joinville, a good portion of the city's production travel's south to the port of Itajai.

- Imbituba is the southernmost port, and the only port located south of the state capital, Florianopolis. Originally, a primary export platform for coal produced in the region, Imbituba experienced hard times in the early 1990s when the coal mines dried up. Imbituba exported 4.11 million tons in 1986 (the peak year of coal production) and only 380,000 tons in 1996. Today, Imbituba exports about 1 million tons (well below 100,000 container units) per year, with its primary cargo being ceramics.

A fifth port, expected to handle mostly meat exports, is currently under construction in the town of Navegantes, near Itajai.

The Port of Itajai: Growth and Challenges

13. An industrial city with a population of 150,000, Itajai is home to the third largest port in Brazil, behind Santos in Sao Paulo state (largest in Latin America) and Rio Grande in Rio Grande do Sul state. Over the past 5 years, the Port of Itajai experienced the second highest percentage of growth in shipping worldwide (only Balboa in Panama grew more), growing 283 percent in container traffic from 2000 to 2005, to 676,800 container units. By way of comparison, Santos had a 2005 volume of over 1.5 million units and

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experienced about 100 percent growth over the same five-year period.

14. The number one export destination for shipments leaving Itajai is the U.S., which received USD 500 million (13.4 percent) of Itajai's USD 3.8 billion total exports. Russia is second, receiving 13.2 percent of all shipments (of which more than 85 percent is meat, mainly pork), followed by Germany, the Netherlands, Japan, and the U.K. (each receiving about 5-7 percent of volume).

15. The huge increase in volume has strained Itajai's existing infrastructure. In 2002, the Brazilian firm Teconvi won a bid to operate the port on a profit-sharing basis with the state government-owned Port Authority of Itajai. Under the lease agreement, Teconvi invested USD 40 million to increase port capacity. By 2008, port expansion will include a new 250-meter berth, 24,000 additional square meters of warehousing (bringing storage to a total of 74,000 square meters), two new tugboats, and three additional container cranes. USD 4 million of the investment is earmarked to build an exclusive access road between the coastal highway (BR 101) and the Port. The GoB has partnered with Teconvi and has committed USD 14 million in federal funds to create this dedicated port access road and freeway exit, since Itajai's increased container traffic has clogged traffic on BR 101, Santa Catarina's principal highway along the populous north-south corridor. (COMMENT. Brazil has yet to harness the efficiencies of multi-modal transport (including rail and waterborne freight). While the Port of Itajai's new access road will improve safety and decrease wait times, it will do little to offset the disadvantages of having a highway-dependent transport route. Infrastructure limitations remain a major hindrance to Brazil's trade expansion. END COMMENT.)

Navegantes: the Port Next Door

16. The contiguous cities of Itajai and Navegantes are separated by the narrow Itajai-Acu River, with the Port of Itajai located on the south shore. Shortly after the CG's visit to the Port of Itajai, construction began on the privately owned Port of Navegantes, which

will be located on the north shore of the Itajai-Acu, directly across from the Port of Itajai. After four years of feasibility studies, the Brazilian firm Portonave is spending USD 180 million to build three berths, along with related support structures and equipment. The City of Navegantes expects to spend USD 12 million on infrastructure (paving roads, providing utility access, etc.). Once operational in October 2007, Navegantes will be the state's second largest port. Portonave expects the Port of Navegantes to create 650 direct and 2,000 indirect jobs during the construction phase, and 250 direct and 1,000 indirect jobs once operational.

¶7. The Port of Navegantes will focus primarily on shipping meat. Santa Catarina is the largest Brazilian exporter of pork products and home to several major meat processing companies, including Seara, Sadia, Perdigao, and Aurora. To attract the meat industry, the Port of Navegantes will include state-of-the-art cold storage warehousing. In a recent interview, Portonave president Carlo Botarelli stated, "Portonave's focus on the meat industry is strategic. It is a sector in which Brazil has great growth potential, despite suffering from sanitary setbacks." (NOTE: While Santa Catarina has not been directly affected, neighboring Brazilian states as well as Argentina and Paraguay have had cases of Foot and Mouth Disease. END NOTE.) Currently, the Port of Itajai is one of the largest shipment points for meat, including the Braskarne Terminal, which is dedicated exclusively to shipments from Seara, a major meat processor. Although the Port of Itajai enjoys a diversified range of cargo (including meat, sugar, ceramics, paper, machinery, chemicals, containers, and wood), the Port of Navegantes will be in direct competition with the Port of Itajai for the meat industry.

PSI: Brazil's First Inbound Cargo Screener

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¶8. The Port of Itajai's recent growth has attracted the attention of U.S. businesses. Port Security International (PSI), a U.S. company based in Reston, VA, recently began non-intrusive container security screening at Itajai. PSI's operations are the first of their kind in Brazil. In September 2005, DHS began its Container Security Initiative (CSI) operations at the Port of Santos in Sao Paulo state, conducting non-intrusive scanning of U.S.-bound containers (ref B). Unlike CSI, PSI focuses on scanning inbound shipments. Inbound scanning is especially attractive to the Brazilian Customs Service given the high incidence of contraband, counterfeit goods, and tariff and tax evasion. PSI's services not only help Customs deter entry of illegal cargo, but also help them recoup otherwise lost tax and tariff revenues. PSI also plans to bid this year on an expected (though as yet unannounced) tender by the Brazilian Customs Service for screening devices and/or services at ports throughout the country.

¶9. COMMENT: Post is encouraged by the Brazilian Customs Authority's interest in container scanning. In recent anti-piracy meetings with Brazilian authorities (including state and local officials in Sao Paulo and Rio Grande do Sul as well as Santa Catarina), CG highlighted foregone tax revenue as one of many motives for Brazil to crack down on piracy. To this end, we think the Port of Itajai's contract for PSI's services is a step in the right direction. While the Port Authority's main incentive is to crack down on contraband and tax/tariff evasion, the seizure of pirated and counterfeit goods will be a natural side effect of screening. END COMMENT.

¶10. This cable was cleared/coordinated with Embassy Brasilia.

McMullen